

VICTOR P. SMITH

IBLA 86-628

Decided February 2, 1988

Appeal from a decision of the Eastern States Office, Bureau of Land management, rejecting the high bid in a competitive oil and gas lease sale. ES 35513 (Miss.).

Affirmed.

1. Oil and Gas Leases: Competitive Leases--Oil and Gas Leases: Discretion to Lease

The Secretary of the Interior has the discretionary authority to reject a high bid in a competitive oil and gas lease sale if the record discloses a rational basis for the conclusion that the amount of the bid was inadequate. The explanation provided must inform the bidder of the factual basis of the decision and must be sufficient for the Board to determine the correctness of the decision if disputed on appeal.

2. Oil and Gas Leases: Competitive Leases--Oil and Gas Leases: Discretion to Lease

The Department is entitled to rely on a reasoned analysis of its technical experts in matters concerning geologic evaluation of tracts of land offered at a sale of competitive oil and gas leases. Where a decision to reject a bid has been made in a careful and systematic manner using the advice of such experts, the decision will not be reversed in the absence of a showing of error.

3. Oil and Gas Leases: Competitive Leases--Oil and Gas Leases: Burden of Proof

When the Government rejects a competitive oil and gas lease high bid because the bid was less than its fair market valuation, the bidder must not only show that there is the lack of a rational basis for the decision or that BLM erred when formulating its fair market valuation, but must also establish that its bid represents fair market value in order to be awarded the lease.

APPEARANCES: Robert T. McElroy, Exploration Manager for Victor P. Smith, Jackson, Mississippi, for appellant.

#### OPINION BY ADMINISTRATIVE JUDGE HARRIS

Victor P. Smith has appealed from a decision of the Eastern States Office, Bureau of Land Management (BLM), dated February 14, 1986, rejecting his high bid for parcel No. 48 (ES 35513 (Miss.)) in the BLM November 21, 1985, competitive oil and gas lease sale. Parcel 48 includes 79.24 acres of acquired land in the West Clara Field Known Geological Structure, described as the SW 1/4 SW 1/4 sec. 3 and the NE 1/4 NE 1/4 sec. 9, T. 7 N., R. 8 W., St. Stephens Meridian, in the De Soto National Forest, in Wayne County, Mississippi. Appellant's \$4,120.50 bid (\$52.00 per acre) exceeded the only other bid, \$2,461.19 (\$31.06 per acre).

On December 13, 1985, BLM sent appellant a notice of probable rejection (notice) of his bid. The notice stated that appellant's high bid was lower than the "presale" estimate of value (PEV) BLM had assigned to the parcel, but BLM did not reveal the PEV figure. BLM allowed appellant 15 days from receipt to submit information to justify his bid.

On December 19, 1985, appellant sent BLM a response to the notice. Appellant stated that he considered the portion of the parcel in sec. 9 merely speculative and noted that he "recently purchased" another lease in sec. 9 for less than \$30 per acre. Appellant submitted three isopach maps of producing horizons: Base Ferry Lake, Top Cotton Valley, and Top Smackover. The maps showed parcel 48 separated by a fault from a zone labeled "prospective area." Appellant's maps show the SW 1/4 SW 1/4 sec. 3 in a field labeled "depleted." He asserted that an oil well on the portion of parcel 48 in sec. 3 had been produced to depletion. Appellant stated that productive wells in the area are deep and expensive to drill. He requested reconsideration of BLM's notice of probable rejection.

On February 14, 1986, BLM issued its decision rejecting appellant's bid because it did not represent fair market value. BLM stated:

The BLM appraised FMV [fair market value] for Parcel No. 48 is \$100 per acre. Your bid was \$52 per acre. The appraised value is based on comparable leasing (sales)

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1/ Appellant's response to the notice was not included in the case file BLM forwarded to this Board. As part of the case record, it should have been. When the Board commenced review of this case and discovered the absence of that document, it requested BLM to forward appellant's response. When BLM did so, it also forwarded additional background information, including a presale geologic report. Nothing in the record indicated that BLM had served this information on appellant, as required by 43 CFR 4.22(b). Therefore, the Board considered it an ex parte communication according to 43 CFR 4.27(b), and by order dated Sept. 30, 1987, forwarded the information to appellant for review. Appellant did not respond.

analysis as set forth in the Uniform Standards for Federal Land Acquisition. This approach was employed because it is considered, when data are available, to be the most reliable and logical indicator of the current market value of mineral interests.

The basic premise of comparable sales analysis is that the market for oil and gas reserves is a competitive situation involving prudent and knowledgeable buyers and sellers. It also assumes that no factors exist to significantly alter the value of the previously leased comparable tract(s) relative to the appraised tract(s). If any such factors exist, they must be accounted for in the final analysis. Some of the most important factors affecting the FMV of the tract's reserves include (but are not limited to): time, location, geology, surface occupancy restrictions, royalty rates, interest rates, and drilling costs. Thus, the best indicators of the current FMV of the Parcel No. 48 are recently-leased tracts with similar geographic, economic and geologic characteristics.

On the basis of the previously stated logic, the best gauge of the FMV of Parcel No. 48 would be a geologically similar Federal parcel offered for competitive leasing at approximately the same time and located in the geographic vicinity of Parcel No. 48. The appraised FMV of Parcel No. 48 is primarily based on the bids submitted for, and BLM appraisal of, Parcel No. 47 of the November 21, 1985 Lease Sales [2/]. The average evaluation of the tract (AEOT) was calculated to be \$95 per acre for Parcel No. 47. An upward adjustment was made in this value because more of Parcel No. 48 than of Parcel No. 47 is located within the known productive limits of the structure and the probability of successfully drilling a commercial well is consequently higher than that for Parcel No. 47, according to BLM geologic analysis. Thus, the appraised FMV of the oil and gas interests of Parcel No. 48 is \$100 per acre.

The geologic analysis performed by BLM for this parcel showed that the West Clara Field is still a producing field, with production coming from the Paluxy, Upper Rodessa and Rodessa Sands (Mississippi Oil and Gas Production Report, June 1985). This productivity is demonstrated by producing wells on two Federal leases (BLM-A-057403-A and BLM-A-077033) adjacent to this parcel. Since these producing wells are on the same side of the major fault highlighted on the maps submitted in response to the NOPR [Notice of Probable Rejection], no other data presented in the response would lead to the conclusion that the West Clara Field is depleted. The fact that

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2/ Parcel 47 was described in the list of parcels as the SE 1/4 NE 1/4 sec. 3, T. 7 N., R. 8 W., St. Stephens Meridian. It is located just north and west of Parcel 48.

the Brandon Company #1 U.S.A. 13-3 well on Parcel 48 is no longer producing from its current depth of 13,820 feet does not preclude the possibility of discovery and production from the other horizons from which wells on adjacent leases are producing. [3/]

(Decision at 1-2).

In his statement of reasons on appeal to this Board, appellant asserted:

You will notice that West Clara Field was discovered in 1966 by Pan American. The highest annual oil production occurred in 1970 when the field made 525,717 barrels of oil. The field presently is making approximately 100 barrels per day and declining. The well closest to Parcel No. 48 is producing 9 barrels per day. The point being, when I referred to the field as "depleted" it is obvious that the field is "substantially depleted" and certainly not economically feasible to drill a new well. We are actually not interested in that part of Parcel 48 lying in Section 3. Our interest is in Section 9 which is farther away from the KGS. Leases of this type which require drilling deep high risk wells typically sell for less than \$50 per acre. The fact that one-half of Parcel 48 is virtually worthless because of depletion further reduces the value of the tract. You will notice that we purchased the ES-034091 lease from Carol Lukawski for less than \$30 per acre. Since this purchase, the price of oil, which directly relates to the value of an oil lease, has dropped over 40 percent (see Ergon Oil Price Bulletins).

(Statement of Reasons at 1-2). Appellant enclosed copies of field and production status data, oil price bulletins and a letter purchase agreement for ES-034091.

[1] The Secretary of the Interior has the discretionary authority to reject a bid for a competitive oil and gas lease if the bid is deemed inadequate. 30 U.S.C. § 226(b) (1982); 43 CFR 3120.5(a); MTS Limited Partnership, 95 IBLA 337 (1987); Michael Shearn, 87 IBLA 168, 169 (1985). This Board has consistently upheld that authority, so long as there is a rational basis for the conclusion that the highest bid does not represent fair market value for the parcel. Eg., Clarence Sherman, 82 IBLA 64, 65 (1984); Viking Resources Corp., 80 IBLA 245, 246 (1986). Departmental policy in the administration of its competitive leasing program is to seek the return of fair

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3/ The Chief, Economic Evaluation, Eastern States Office, BLM, included this postsale analysis of Parcel 48 in a Jan. 22, 1986, memorandum to the Chief, Branch of Minerals Adjudication, Eastern States Office, BLM. In the memorandum he recommended the inclusion of the rationale in the decision.

market value of the grant of leases, and the Secretary reserves the right to reject a bid which will not provide a fair return. Viking Resources Corps, *supra* at 246.

[2] When exercising the Secretary's authority to reject a high bid, the Department is entitled to rely on the reasoned analysis of its technical experts in matters involving geologic evaluation of tracts of land offered at a sale of competitive oil and gas leases. Viking Resources Corp., *supra* at 247; L. B. Blake, 67 IBLA 103 (1982). However, when BLM relies on that analysis, it must ensure that a reasoned explanation to support the decision is provided in the record. Mesa Petroleum Co., 81 IBLA 194, 195 (1984). If the record indicates a decision to reject a bid has been made in a careful and systematic manner utilizing the advice of such experts, that decision will not be reversed, absent a showing of error, even though the determination may be subject to reasonable differences of opinion. See *Kerr-McGee Corp. v. Watt*, 517 F. Supp. 1209, 1213-14 (D.D.C. 1981).

At the time BLM issued its decision rejecting appellant's bid, BLM did provide a reasoned explanation in the record to show a rational basis for its conclusion that appellant's bid for parcel 48 did not represent fair market value. In its postsale analysis, BLM estimated the value of parcel 48 to be \$100 per acre, almost double appellant's bid of \$52 per acre. BLM used a comparable sale approach and a comparison of three nearby wells to reach this conclusion. Appellant's assertion that he purchased a lease containing acreage in sec. 9, T. 7 N., R. 8 W., St. Stephens Meridian, for \$30 per acre does not establish that BLM's estimate of value was in error. The purchased lease (ES-034091) contains acreage scattered over at least seven sections. The lump sum purchase price reflects the average price per acre paid by appellant for all the land in ES-034091. Appellant has not shown how the \$30 per acre average price specifically relates to the acreage in sec. 9.

Although the Board has held that BLM should provide a rational basis for its determination to reject a high bid, we have also concluded that even where BLM fails to provide a rational basis for its rejection decision or where the high bidder shows BLM has erred in its determination of a minimum acceptable bid value, the high bidder must establish that his bid represents fair market value in order to be awarded the lease. *Miller Brothers Oil Corp.*, 100 IBLA 172 (1987); *Burton/Hawks, Inc.*, 98 IBLA 118, 122 (1987); *Southern Union Exploration Co.*, 97 IBLA 275, 277 (1987).

In essence, appellant is arguing that BLM's fair market valuation of parcel 48 does not take into consideration the risk and expense of drilling deep wildcat wells. He realizes there are producing wells in the vicinity of parcel 48, but intimates that their low production rates support his position that the field is substantially depleted.

The record clearly shows the West Clara is still a producing field. BLM acknowledges the existence of the depleted well on the sec. 3 portion of parcel 48, but the BLM geologic report states that there are seven different producing zones in the field, and BLM asserts that depletion of that well at its current depth does not preclude the possibility of discovery and production from another horizon.

BLM utilized comparable data generated in the November 1985 sale to derive its post-sale fair market valuation for parcel 48. It also prepared a geologic report which contains information supporting its action. Thus the record establishes that BLM made a reasoned analysis upon which the Department may rely. Appellant's submissions are not sufficient to show any error in BLM's decision.

Accordingly, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision of the Eastern States Office, BLM, is affirmed.

Bruce R. Harris  
Administrative Judge

We concur:

Wm. Philip Horton  
Chief Administrative Judge

John H. Kelly  
Administrative Judge

